

**EXAMINATION OF THE  
KENTUCKY AGRICULTURAL DEVELOPMENT BOARD -  
ALLIED FOOD MARKETERS WEST, INC. PROJECT**



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## **CONTENTS**

	<b><u>Page</u></b>
<b>TRANSMITTAL LETTER .....</b>	<b>1</b>
<b>BACKGROUND .....</b>	<b>3</b>
<b>FINDINGS AND RECOMMENDATIONS .....</b>	<b>4</b>
<b>EXHIBITS</b>	
<b>EXHIBIT A - Allied Food Marketers West, Inc. Schedule of Grant Receipts     and Expenses For the Period March 1, 2005 Through March 31, 2008 .....</b>	<b>18</b>
<b>EXHIBIT B - Allied Services Provided to Kentucky Producers .....</b>	<b>23</b>
<b>AGENCY RESPONSE .....</b>	<b>33</b>





CRIT LUALLEN  
AUDITOR OF PUBLIC ACCOUNTS

August 15, 2008

Members of the  
Kentucky Agricultural Development Board

Roger Thomas, Executive Director  
Governor's Office of Agricultural Policy  
404 Ann Street  
Frankfort, KY 40601

RE: KADB Project - Allied Food Marketers West, Inc.

Dear Board Members and Mr. Thomas:

We have completed our examination of the Kentucky Agricultural Development Board's (KADB) project related to Allied Food Marketers West, Incorporated (Allied) for the period May 31, 2005 through March 31, 2008.

Examination procedures included reviewing the contract between KADB and Allied; analyzing detailed financial information, including subcontractor costs; conducting interviews of members of the KADB, current and previous GOAP employees, employees of Allied, as well as other parties professionally associated with this project; and analyzing business relationships between Allied, its subcontractors, employees of GOAP, and members of KADB for possible conflicts of interest.

Findings in this report include:

- KADB's contract with Allied was not sufficient to protect the Commonwealth's interest in multiple areas;
- Conflict of interest existed in Allied's second KADB contract;
- GOAP did not have adequate monitoring procedures in place to detect or prevent grantee misappropriation during the period under examination;
- GOAP does not have adequate documentation procedures in place to ensure project modifications are properly noted and communicated to KADB.



Kentucky Agricultural Development Board  
Roger Thomas  
Page 2  
August 15, 2008

Detailed findings and recommendations based on our examination are presented in this report to assist KADB and GOAP in improving procedures and internal controls.

Very truly yours,

A handwritten signature in black ink, appearing to read "Crit Luallen", with a long horizontal flourish extending to the right.

Crit Luallen  
Auditor of Public Accounts

## **Background**

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The Kentucky Agricultural Development Board (KADB) was created in 2000 by KRS 248.707 to administer the agricultural development fund, which was established to use receipts from the Tobacco Master Settlement Agreement to provide economic assistance to the agricultural community of Kentucky. The Governor's Office of Agricultural Policy (GOAP) provides administrative support to KADB.

KADB, with the assistance of GOAP and the Kentucky Department of Agriculture (KDA), identified missing links in the process of aiding Kentucky producers reach consumers in retail markets, and charged GOAP staff with the task of finding a project to help meet those needs. Since this was a new venture for KADB, there was no previous project to serve as a model, and no known vendors offering this type of service. KADB charged GOAP management with the task of recruiting businesses or individuals outside of state government to meet this need. GOAP helped identify Allied Food Marketers West, Inc. (Allied) as a possible candidate, and entered into discussions with Allied on the scope and viability of the project, which ultimately resulted in an application by Allied for funding submitted to KADB. In May 2005, KADB approved funding of the new project (application A2005-093) with Allied. Allied's application outlined its proposal to implement a program to assist Kentucky producers with the following services: create a business development model to help producers explore the viability of products and identify and develop viable business plans; provide educational tools for producers, distributors and end users; develop distribution and merchandising models; and create sound technical and data platforms, such as development of a website, for producers and end users. These objectives were also intended to support KDA's Kentucky Proud program by filling a missing link by consulting with and educating producers how to move their business into retail markets, and by providing the contacts necessary for that to occur. The initial legal agreement was part grant in the amount of \$1,977,661 and part forgivable loan in the amount of \$1,013,900, with a two-year term ending June 30, 2007.

In December 2006, KADB approved Allied for a third year of grant funding (application A2006-0412) in the amount of \$1,900,000. The agreement contained an earmark agreement that required \$500,000 of the total to be paid for the Rebekah

Grace Food Supplements For Life, LLC (Rebekah Grace) initiative (application A2006-001), a company that labels and markets products for natural and organic producers. In this agreement, KADB also approved the conversion of Allied's original forgivable loan to a grant. The third year of funding extended Allied's project through June 30, 2008, increasing the total grant award to \$4,891,561, \$500,000 of which was to be paid to Rebekah Grace. A schedule of Allied's grant receipts and expenses applied against the grant is included in Exhibit A.

Although KADB minutes appear to indicate KADB approved the contract based on Allied's previous experience in the food industry, Allied did not maintain significant business operations outside of the grant, and the KADB funding became Allied's primary source of revenue during the course of the project. In the first calendar year the contract was in place, state funding constituted 75.5% of Allied's revenue source. In the second and third calendar years of the project, state funding represented approximately 81% and 96% of Allied's total revenues, respectively, with Allied's remaining revenue source primarily being commission earnings, some of which was derived from producers connected with this project. It is important to note that because of the level of Allied's funding derived from state resources, and because its primary objectives were established from a state grant initiative, this did not appear to be a contractual relationship in which the Commonwealth paid for services provided by a business engaged in the same work for other clients. Instead, the Allied project basically established an entity that operated more like a program of the Commonwealth due to the business's financial dependency on this grant. Even though this fiscal dependency existed, KADB intended for Allied to operate as a separate non-governmental business entity with no authority to obligate any state agency for funding or services.

## **Findings and Recommendations**

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### **Contracts with Allied did not adequately protect the Commonwealth's interest**

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KADB entered into two separate legal agreements with Allied between May 31, 2005 and June 30, 2008. The first agreement was for the first two years of funding, while the second agreement provided for the third year of funding as outlined previously. We identified several provisions that were not included in either one or both contracts, which would have better protected the interest of the Commonwealth.



*A termination clause was not included in the first contract.*

The first contract did not contain a termination provision. Other KADB contracts, including the second contract with Allied, contain a clause to permit contract termination with written notification to the grantee. 200 KAR 5:312 permits the Commonwealth to terminate contracts in the event of default or at the convenience of the Commonwealth, which allows the agency to react to budgetary constraints, performance concerns, and other events. It is important that these provisions are clearly communicated to all parties in the contract.

*Conflict of interest or related party transactions were not prohibited.*

Neither contract included a conflict of interest provision, and did not address related party transactions, which could indicate the existence of potential conflicts. These provisions would require grantees to avoid entering into business arrangements that create a conflict of interest, and to disclose in advance and/or gain approval for transactions or agreements with related parties. Related parties may be relatives of the business's management, or arrangements with businesses or other entities in which an officer or employee holds a significant financial interest.

*Prior approval or cost estimates were not required for more than \$681,782 paid to subcontractors, \$374,970 of which was paid to related parties.*

Neither contract required approval or disclosure of subcontractors. Board minutes indicate Allied's intent to use subcontractors was discussed with KADB, but we could not determine that all subcontractors and the nature of their work combined with estimated costs were presented for consideration or approval. This information would provide KADB opportunities for more informed decision-making about the direction of the project and provide greater oversight capabilities. During the course of the project, \$681,782 in subcontract arrangements were made by Allied, which included both an hourly rate paid for services plus expenses. Of that amount, more than \$374,970 was paid to related party subcontractors, with approximately \$357,570 paid to a single subcontractor operating under two different business names during the contract period.

*Billable charges were not outlined in writing, leading to charges that appear to be unnecessary or unreasonable for the project.*

Neither contract provided specific guidance, directly or by reference, on spending limitations or billable charges. Certain expenses that would normally be identified as unnecessary or unreasonable for the project were not prohibited. Examples of these practices that were not identified in writing in the contract included:

- Based on Allied's understanding of verbal agreements made during the contract negotiation, Allied was permitted to charge both an hourly rate for billable hours and actual

expenses against the contract. Therefore, Allied submitted expenses for mileage, travel, meals and entertainment and other expenses, on top of a negotiated rate of \$250 per hour for program administration. Allied also paid subcontractors' expenses on top of agreed upon hourly rates in many cases. The contract detailed the payment frequency for Allied's grant funding, but did not detail the billable charges or identify whether expenses should be built into the hourly rates.

- Allied spent approximately \$56,000 on charitable contributions and sponsorships during the project period. These contributions and sponsorships included:
  - \$4,750 contributions for retailer-sponsored golf tournaments, and another \$250 for an out-of-state golf tournament;
  - \$1,425 in booster club donations to the high school attended by one of Allied's officers; and
  - \$33,600 sponsorship for 56 retail employees to attend a meat cutter's training school, 26 of whom were out-of-state residents.
- Approximately \$15,400 was spent for meals and snacks for Allied employees and/or subcontractors that would not normally be considered necessary or reasonable, such as:
  - \$3,882 in meals between one Allied officer and his spouse, a subcontractor of the project; and
  - \$1,735 in employee lunches during Allied staff meetings;
  - Over \$9,700 in other meals in which the reasonableness of the meal was questionable due to excessive costs for the circumstance, excessive gratuities including one instance in which a \$70.49 tip was left for a purchase totaling \$44.51 (158%) and another instance in which a \$70.03 tip was left for a \$29.97 purchase (233%), and meals for purposes that did not appear to advance the project objective.
- \$80,000 loan paid to a retailer to advance money owed by KDA. The funds were repaid by the retailer the following month.
- Time charges and expenses for participation in the Kentucky Agricultural Leadership Program.

*Additional fees charged to producers were not prohibited.*

Neither contract provided limitations on fees and commissions that could be charged by Allied to Kentucky producers intended to be served by the project. Allied entered into arrangements for commissions with some, but not all, producers for brokerage services. This raised questions from producers and others familiar with this project regarding what services were covered by the KADB contract. KADB meeting minutes indicate discussions were held regarding the self-sustainability of Allied in the future, but there did not appear to be a clear understanding of when the charges for other services would begin or what services those fees would include, leaving Allied to establish its own fee structure. No clear criteria were set for the commissions, but the focus was producers with the best chance for long-term feasibility. Allied indicated its commissions were never mandatory for any producer.

*The authority for project management and oversight was not clearly defined in the contract.*

Neither contract provided clear authority for oversight and management of the project. Because Allied was working to advance the Kentucky Proud program, a KDA trademarked initiative, there was a natural inclination by KDA to manage this project. Although it appears KDA helped manage the project in the beginning, GOAP ultimately retained control for oversight and accountability. If KDA was to have any responsibility in overseeing the objectives related to its own program, those terms were not clearly defined in the contract.

### *Recommendations*

We recommend KADB legal agreements include provisions that will provide greater protection and oversight capabilities, including the following:

- Termination clause;
- Conflict of interest statements, including limitations on transactions with related parties;
- A requirement for preapproval of subcontractors, with scope and cost estimates;
- Agreements related to billable charges and fee arrangements, listed in the contract or incorporated by reference to a separate document;
- Clearly defined roles and responsibilities of all parties, including project management and oversight authority;
- Measurable accountability standards.

### **A conflict of interest existed between Allied and Rebekah Grace**

A conflict of interest exists when an organization, its officers or its employees has a financial interest in another organization with which it does business. The second legal agreement entered into between Allied and KADB included funding in the amount of \$500,000 for Rebekah Grace. The general manager of Rebekah Grace was also an employee of Allied.

Furthermore, Allied and Rebekah Grace entered into a brokerage agreement, which indicates Allied benefited directly from sales generated by Rebekah Grace. Since Allied's role was to consult with producers to determine the most viable options for marketing their products, a conflict existed when working with all natural and organic producers because Allied had an inherent vested interest in the success of Rebekah Grace and could potentially earn more if the producer sold products under the Rebekah Grace label as opposed to their own label or other alternatives.

### *Recommendations*

We recommend KADB avoid contractual arrangements that create potential conflicts of interest. If applicants can provide sufficient evidence that a conflict of interest can be overcome, the justification for approval, as well as additional oversight measures should be approved by legal counsel and documented in the project file.

To further reduce the risk of potential conflicts of interest, we also recommend that GOAP maintain a file for each of its employees of all external personal and financial conflicts of interests in the agriculture industry. These files should be utilized to ensure that no project analyst or other employee be assigned to projects in which they have a real or perceived conflict of interest.

### **Decisions and approvals related to the scope and direction of the Allied project were not documented**

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Because the Allied project was a new concept and no previous model existed, it appears the objectives were intentionally broad in order to give latitude to build the project. Over time, the project's scope expanded into other areas not documented in the legal agreements, such as organizing trade shows and conducting significant amounts of agricultural research, much of which was completed with the assistance of subcontractors.

### *Allied communicated day-to-day activities to GOAP management verbally.*

It appears Allied's day-to-day activities, including those projects which appear to expand the original agreement, were reportedly communicated to and approved by GOAP management verbally, and in some cases significant projects were also communicated to KADB in monthly executive summaries presented by Allied. However, there is no documentation of approvals, even those that may have expanded the scope of the project, which constituted a modification of the legal agreement.

*Approvals were made without project cost estimates or other financial considerations.*

Furthermore, it does not appear GOAP management utilized financial considerations when approving the day-to-day activities, and thereby may not have had a clear understanding of the costs of the projects approved. Examples of this type of project work reportedly communicated and approved by GOAP management include:

- Hydroponic tomato project, which researched the development of a business model to share with multiple Kentucky producers for hydroponics growing operations. Significant staff time was billed to this project, and approximately \$146,545 in additional subcontractor costs were charged between August 2006 and March 2008 from three separate subcontractors. Based on information reported in Allied's monthly executive summaries to the KADB, this project was active throughout the period under examination, and reportedly resulted in increased sales of hydroponic tomatoes grown in Kentucky.
- Horticulture research project, which researched the viability of using tobacco barns as storage green houses for container plants. Subcontractor charges for this project were approximately \$100,000 between February 2007 and August 2007. This project reportedly was not deemed to be viable.
- 2007 Kentucky Proud Expo, which was coordinated by Allied to draw retailers and producers together in one arena. In addition to significant staff time and expense charged to this program, Allied also utilized a subcontractor, who was paid \$59,375 for Expo-related event planning and coordination in 2007.

### *Recommendations*

We recommend GOAP management and project analysts document all significant decisions and approvals made with project applicants. In order to facilitate this additional documentation, we recommend GOAP institute a project log sheet to be used during each phone conversation and meeting with applicants and recipients. It is not necessary to document routine discussions, but all conclusions that modify the scope or clarify definitions of the legal agreement should be documented and maintained on file.

We also recommend management and project analysts document cost estimates of any modifications approved, and GOAP management establish a policy for modifications that require input from general counsel and/or the executive director.

**GOAP and KADB did not have sufficient monitoring procedures in place to define and detect questionable spending practices**

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In order to monitor projects for financial accountability, as well as determine whether projects are meeting their contractual obligations, it is important to have proper monitoring procedures in place. Based on board minutes and interviews with current and former GOAP employees and KADB members, KADB established more reporting requirements for Allied than for other projects at the time. However, weaknesses still existed that created barriers to effective monitoring of this project.

*Guidance was not given on disallowed expenses.*

Allied was not provided with guidance on disallowed expenses. Due to the varied nature of projects approved by KADB, a single list of *allowable* costs may be difficult to define. However, *disallowed* costs and other limitations should be similar for all projects, but have not been defined by GOAP. The list can be modified for specific projects if KADB deems certain expenses to be reasonable for a given project.

*GOAP compliance function was not adequately staffed.*

GOAP did not have sufficient compliance staffing levels to review detailed financial information. During much of the contract period from May 2005 through December 2007, only two compliance officers were on staff with GOAP who were responsible for ensuring that each KADB project had met its reporting requirements before a payment was processed. This level of staffing was insufficient for detailed financial monitoring of the number of projects approved by the KADB.

*Required quarterly reports did not contain meaningful data for financial monitoring.*

The quarterly reports required by Allied are not sufficient for monitoring. The reports provided budget to actual detail, but additional financial information more conducive to desk-review procedures of expenses was not required. Therefore, even if compliance officers had time for more thorough reviews, the information would not be meaningful for financial and/or compliance monitoring.

*GOAP did not review monthly detailed expense reports submitted by Allied.*

Even though not required, Allied submitted monthly expense reports to GOAP containing time charges, as well as detailed invoices and receipts billed to the project. The reports were not routinely submitted at regular intervals, but in some cases were submitted in batches of several months at a time. Based on interviews with former and current GOAP employees, since these reports were not required by contract, and also because of limited compliance staffing, these expense reports were filed without any type of review. Had GOAP reviewed these expense reports, it is likely that questions regarding Allied's spending practices would have arisen, such as those noted in the contract spending limitation finding of this report.

*Receipts indicate state employees may have received financial benefits from Allied in the form of meals and other expenses.*

Our review of detailed expenses also identified instances in which it appears state employees were provided meals and other expenses paid by Allied. KRS 11A.045 (1) states “No public servant, his spouse, or dependent child knowingly shall accept any gifts or gratuities, including travel expenses, meals, alcoholic beverages, and honoraria, totaling a value greater than twenty-five dollars (\$25) in a single calendar year from any person or business that does business with, is regulated by, is seeking grants from, is involved in litigation against, or is lobbying or attempting to influence the actions of the agency in which the public servant is employed or which he supervises, or from any group or association which has as its primary purpose the representation of those persons or businesses.” Since employee names were not always identified, and because records were not always sufficient to calculate the amount of the benefit received by state employees, we were unable to determine whether any single employee received more than \$25 in a given year. We did not find evidence indicating that these activities were routine; however, as a general rule, state employees should refrain from accepting meals and other items provided by grantees and vendors that are not offered to the public at large.

*No one agency had the information necessary for proper oversight.*

KDA was not given an official role in monitoring and providing routine feedback related to this project. Because Allied’s objectives related to Kentucky Proud, and the close, day-to-day contact between KDA, producers, and Allied, KDA was in a good position to help evaluate Allied’s progress. However, financial accountability and project management rested with GOAP. Due to the organizational impairments of having the project objectives impact a different agency than the agency responsible for accountability, no one agency had the full perspective needed to provide proper oversight.

### *Recommendations*

We recommend GOAP improve monitoring procedures by:

- Developing a checklist for each project file to document the monitoring procedures outlined and performed for that specific project. The checklist can be tailored to the type of project and dollar amount of funding awarded, and include a variety of monitoring procedures and accountability measures, such as a review of the standard quarterly/annual reports for budgetary review, periodic on-site monitoring, inspection of a sample of detailed receipts, and a final project report that provides an overall project evaluation.

- Documenting a list of unallowed expenses and establishing guidelines for reasonable and necessary expenses, and providing this information to all project applicants. This list should be periodically reviewed, updated, and modified based on the type of contract as needed.
- Expanding the staffing resources for compliance-related functions to devote more time for detailed monitoring. GOAP may consider part-time assistants or interns to help with model programs, and consider utilizing project analysts for some monitoring functions outside of their own district assignment to maximize the use of its workforce. Project analysts should not be assigned to monitor projects within their own district.

We also recommend GOAP communicate clear expectations regarding the acceptance of gifts and gratuities, including meals, in order to ensure compliance with KRS 11A.045. This policy should be communicated to all GOAP employees, as well as to KDA and other state agencies receiving KADB funding.

**The impact of the Allied project is not readily quantifiable due to the lack of established accountability measures, and appropriate project evaluations**

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In attempting to evaluate Allied's contract performance, the Auditor of Public Accounts (APA) identified three primary contract objectives based on a review of the written contracts and various interviews performed. The contract objectives identified and considered were a) creation of a business development model to help producers explore the viability of products and identify and develop viable business plans; b) provision of educational tools and creation of technical and data platforms, such as development of a website, for producers and end users; and c) development of distribution channels to assist producers in getting products to retailers.

*KADB's project with Allied opened retail avenues for producers that did not previously exist, but overall success of the project is difficult to determine.*

State agencies have procurement limitations in their ability to contract with specific retailers to close the gap for producers, which is why the Allied project was considered to be necessary by KADB. During our examination, there appeared to be consensus among various individuals impacted by this project that Allied did open up retail avenues for Kentucky producers that did not previously exist. When asked to provide documentation of the results of its project work, Allied identified a list of 187 producers in which it provided consultation and/or product placement services, and noted 18 retail chains to carry products of these Kentucky producers. This list of producers and services was provided by Allied and



has not been independently verified by the APA, but has been provided for informational purposes (Exhibit B). The ultimate result of this objective should be increased farm gate receipts for producers. However, due to limited required accountability measures, information is not available to readily determine Allied's overall success in meeting this objective.

*A website providing a linkage from producers to markets of consumers was made available to Kentucky producers through a partnership between KDA, UK, GOAP and Allied.*

During the first few months of the project, Allied's monthly executive summaries indicate work performed on website development, to create an online tool it was to provide under this contract. However, this need was met through MarketMaker, a mapping website initially developed by the University of Illinois which Kentucky joined through a partnership between KDA, University of Kentucky (UK), GOAP and Allied. The website contains locations of businesses and producers, census information, and other tools to help provide a link from Kentucky producers to the consumer.

*Allied's objective of providing distribution channels was slow to progress.*

The final objective considered by the APA in assessing contract performance related to opening distribution channels for Kentucky producers. During the first two years of funding, we could not determine that any progress was made in opening distribution channels. There appeared to be a greater emphasis on working toward this objective in the third year of funding based on Allied's summaries submitted to KADB, but there was not enough information available to analyze performance since the information reported by Allied contained only status updates for distribution leads, without service volume or sales data.

Ultimately, even though evidence exists that Allied's project did open retail avenues that could not be provided by a state agency, the project's cost-benefit is not readily determinable due to the lack of required accountability measures, the lack of written documentation for project modifications, and the weaknesses identified in monitoring the project.

### *Recommendations*

We recommend KADB and GOAP make improved monitoring and project accountability a priority. The lack of reliable financial data made it difficult for KADB to meet its statutory requirement noted in KRS 248.709 of developing criteria to evaluate the success of the board's programs. KADB made a positive step toward improved accountability by implementing a quarterly recipient review committee for Allied. However, this committee did not receive adequately detailed information to provide strong oversight. Also, by meeting with Allied

quarterly, the committee could not make timely decisions had they become necessary, and thus is dependent upon GOAP providing more routine monitoring and communicating serious concerns in the interim.

KADB minutes indicate that it has also requested an investment impact study through the University of Kentucky, which is due to be released later this year. The impact study will likely provide the KADB additional information regarding the impact of various investments, including the Allied project.

## **EXHIBITS**



**EXHIBIT A**

**Allied Food Marketers West, Inc.**  
**Schedule of Grant Receipts and Expenses<sup>1</sup>**  
**For the Period March 1, 2005 Through March 31, 2008**

	<u>Totals</u>	
<b>RECEIPTS:</b>		
Grant Funding	\$ 4,283,129	
<b>Total Receipts</b>		<b>\$ 4,283,129</b>
<b>EXPENSES:</b>	<b>Fees</b>	<b>Expenses</b>
<b>Subcontractors:</b>		
Adam Tabor	100	\$
Bill LeGrand	613	342
Bill McCord	24,431	7,245
Bisig Impact Group	2,650	
Bob Perry	460	89
Brandi Nall	11,237	1,589
Chef Gil Logan	3,300	140
Chef Nancy	587	258
Debra Nall	12,045	136
Derrick Riddle	24,400	
Four Seasons Nursery	194,178	5,244
GSL Consulting	5,700	
Kentucky Marketing Solutions	2,310	1,784
Larry Stettenbenz	6,057	169
Midwest Culinary Institute	450	
No Bark All Bite	241,094	
Rebekah King	720	232
Red7e	240	
Ron Raque	2,732	458
Schneider DeMuth Advertising	750	
Shelf Solvers Inc.	115,276	1,200
Southern Delight Gourmet Foods		282
Videobred	3,920	200
WD King	7,893	1,271
<b>Total Subcontractor Expenses</b>	<b>661,143</b>	<b>20,639</b>
		681,782

**Allied Food Marketers West, Inc.**  
**Schedule of Grant Receipts and Expenses<sup>1</sup>**  
**For the Period March 1, 2005 Through March 31, 2008**

	<u>Fees</u>	<u>Expenses</u>	<u>Totals</u>
<b>Other Expenses:</b>			
Meals & Entertainment		73,318	
Mileage		90,373	
Advertising/Marketing		82,345	
Contributions/Charity		5,556	
Food Shows		85,342	
Product Samples		10,155	
Miscellaneous		108,389 <sup>2</sup>	
Cell phone		16,632	
Professional Fees		107,174	
Rebekah Grace		375,000	
<b>Total Other Expenses</b>		<u>954,284</u>	954,284
 <b>Program Administration</b>	 <u>2,647,063</u>		 2,647,063
 <b>Total Expenses</b>			 <u><b>4,283,129</b></u>
<b>REMAINING BALANCE</b>			<u><u><b>\$ 0</b></u></u>

<sup>1</sup>Schedule compiled from Allied monthly expense reports. The amounts were examined for the purposes of this report, but are unaudited. Even though Allied's contract began May 31, 2005, expenses were submitted for the period March 2005 - May 2005 for expenses incurred during that period related to planning and preliminary work. The schedule ends on March 31, 2008 because expense reports for April-June were not available due to the timeframe of the examination.

<sup>2</sup>Miscellaneous expenses includes an amount for sponsorships cited in the report.

<sup>3</sup>Total Program Administration expenses represent the amount of billable hours charged against the grant based on available funding. Allied submitted billable hours totaling \$6,251,344, but per its accounting policy, reimbursable expenses are applied first and then billable hours are applied to the extent grant funding remains.

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**EXHIBIT B**



**APA Disclaimer:**

*The information presented in this exhibit was requested by the APA in the course of our examination. Through inquiry, we determined detail records of services performed under the Allied contract were not maintained, and were not required to be reported under the contract. Therefore, Allied employees prepared the following schedule at the time of our request as their representation of services provided to Kentucky producers. This schedule was not independently verified by the APA.*

County	Producer	Services		Retailers	Total Retail Stores	*
		Consultant	Product Placement			
Allen				[Refer to legend on last page.]		
	John Habegger	✓	✓	K,L,H,R,V,T,N,WF,U,P,I	255	
	Zimmerman Families	✓	✓	K,L,H,R,V,T,N,WF,U,P,I	255	
	Bill Hoover	✓	✓	K,L,H,R,V,T,N,WF,U,P,I	255	
	Mazeline Families	✓	✓	K,L,H,R,V,T,N,WF,U,P,I	255	
	Weaver Families	✓	✓	K,L,H,R,V,T,N,WF,U,P,I	255	
	Irving Miller	✓	✓	K,L,H,R,V,T,N,WF,U,P,I	255	
	Imhoff Families	✓	✓	K,L,H,R,V,T,N,WF,U,P,I	255	
	Spring Valley Farms	✓	✓	K,L,H,R,V,T,N,WF,U,P,I	255	
	Johnathon Hoover	✓	✓	K,L,H,R,V,T,N,WF,U,P,I	255	
	Johnathon Habegger	✓	✓	K,L,H,R,V,T,N,WF,U,P,I	255	
	Beachy Family	✓	✓	K,L,H,R,V,T,N,WF,U,P,I	255	
	Glick Families	✓	✓	K,L,H,R,V,T,N,WF,U,P,I	255	
	Troyer Families	✓	✓	K,L,H,R,V,T,N,WF,U,P,I	255	
	Andy Habegger	✓	✓	K,L,H,R,V,T,N,WF,U,P,I	255	
Barren						
	Billy Joe Williams	✓	✓	H,V,	8	
	Carl Chaney	✓	✓	U,I	2	
	Kenny Mattingly	✓	✓	K,R	11	
Bath						
	Billy Webb	✓	✓	R,I	3	
Boone						
	Boone County Cons Dist	✓				
	Jimmy Scott	✓				
	Bob Murphy	✓				
	Don Talbert	✓				
	Kenman Farms	✓				
	Marilyn Baker	✓	✓	V	5	
	Eddie Gipson	✓				
	Mark Balasa	✓	✓	CP	5	
	Millard Long	✓	✓	K,L,H,W,S,R,V,T,N,WF,P	352	
	Gary Nelson	✓	✓	K,R,V,WF	35	
	Steve Brooks	✓				
	Robert Carl	✓	✓	K,L,H,R,V,T,N,WF,U,P,I	261	

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## Allied services provided to KY Producers (along with associated Retail locations)

...continued...

County	Producer	Services		Retailers	Total Retail Stores	*
		Consultant	Product Placement			
[Refer to legend on last page.]						
Bourbon						
	Billy Gatton Jones	✓	✓	S,C	82	
	Butch Case	✓	✓	K,R,I,V,P	205	
	Dana Reed	✓				
	Mingua Bros	✓				
	Tom Preston	✓				
Boyle						
	Elmwood Inn	✓				
	David Kleckner	✓	✓	H,R,V	12	
Bracken						
	Mac McAlonan	✓	✓	R	7	
	Mary Ellen Stegeman	✓				
	Sheila Desimo	✓				
	Everet Hopkins	✓				
	Garvis Woods	✓	✓	C,G	2	
	McDowell Family	✓	✓	V,I	9	
Butler						
	Bobby Lindsey	✓				
	10 Harvestland Family Growers	✓	✓	K,W	397	
Calloway						
	Ellis Family	✓	✓	L,S,,R,V,T,	155	
Campbell						
	Larry Leap	✓				
Carroll						
	Les Ball	✓				
Carter						
	Chris Johnson	✓				
Casey						
	Yoder Family	✓				
Christian						
	3 Harvestland Family Growers	✓	✓	K,W	397	
	Ernie hampton	✓				
	Charles Petty	✓				

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## Allied services provided to KY Producers (along with associated Retail locations)

...continued...

County	Producer	Services		Retailers	Total Retail Stores	*
		Consultant	Product Placement			
[Refer to legend on last page.]						
Clark	Karen Perkachik	✓				
	McCord Farm	✓	✓	I	2	
	Richard Van Sickle	✓				
	Zeldon Angel	✓	✓	K,R,V,	187	
Daviess	Kevin Trunnel	✓	✓	I	1	
	Rod Kuegel	✓	✓	K	3	
	John Kuegel	✓				
	14 Harvestland Family Growers	✓	✓	K,W	397	
Fayette	Bill Madden	✓	✓	R,V,I	15	
	Creech Services	✓				
	Jeff Roark	✓				
Fleming	John Adams	✓				
Franklin	Pete Mattox	✓				
	Steve Skelton	✓				
Fulton	Sam Hancock	✓				
Gallatin	Bill LeGrand	✓				
	Harmon Brothers	✓				
Garrard	Bluegrass Lamb and Goat	✓	✓	I	1	
	Ernie Kidd	✓				
	Stan Pace	✓				
	Joe Montgomery	✓	✓	R	7	
	Karen Rasmussen	✓				
Grant	Rodney Stevenson	✓	✓	I	1	
	Steve Gregory	✓	✓	I	1	
	Gary Oaks	✓	✓	I	1	

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## Allied services provided to KY Producers (along with associated Retail locations)

...continued...

County	Producer	Services		Retailers	Total Retail Stores	*
		Consultant	Product Placement			
[Refer to legend on last page.]						
Grayson	8 Harvestland Family Growers	✓	✓	K,W	397	
Green	Phil heiskell	✓	✓	H,R,V,.C,I	45	
	David Givens	✓	✓	H,R,V,.C,I	45	
	Ed Rogers	✓	✓	H,R,V,.C,I	45	
	Robert Conley	✓	✓	H,R,V,.C,I	45	
	Jackie Bowen	✓	✓	H,R,V,.C,I	45	
Hancock	Dan Smith	✓				
Harrison	Bill McCord	✓	✓	I	1	
	Brian Furnish	✓				
	C & W Meats	✓				
Hart	Annie miller	✓	✓	H,R,V	18	
Henderson	Jim Baird	✓	✓	L,M	95	
	Thomas Family	✓				
Henry	Paul Tokosh	✓				
Jefferson	Joe Mcneeley	✓				
	Lewis Schuckman	✓	✓	R,	7	
	George Gagel	✓	✓	I,C,WF,R,V,K	5	
	Gene Hewitt	✓				
	Bill Doan	✓	✓			
	Bill Kamer	✓	✓	I	10	
	John Hassmann	✓	✓	I	1	
	Eugine Stratton	✓				
Jessamine	Chris Nelson	✓	✓	K,I,C	9	
	Pearse Lyons	✓	✓	I	6	
	Connie Rogers	✓	✓	R,V	12	
	Chris Evans	✓	✓	K,R,V,I	190	
	Henkel's Tomatoes	✓				

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## Allied services provided to KY Producers (along with associated Retail locations)

...continued...

<u>County</u>	<u>Producer</u>	<u>Services</u>		<u>Retailers</u> <i>[Refer to legend on last page.]</i>	<u>Total Retail Stores</u> *
		<u>Consultant</u>	<u>Product Placement</u>		
<b>Knox</b>	Greg Mitchell	✓	✓	S	81
<b>Larue</b>	Gil Meyers	✓			
	Mark Lee	✓			
<b>Laurel</b>	Bill Wood	✓			
<b>Lincoln</b>	Lincoln County Produce Auction	✓	✓	V	5
<b>Logan</b>	Willis Schrock	✓	✓	R,V,WF,NI,I	42
	Fairview Produce Auction	✓			
<b>Lyon</b>	Ronnie & Beth Drennan	✓	✓	K,R,V,C,I	90
<b>McClean</b>	50 Harvestland Family Growers	✓	✓	K,W	397
<b>Madison</b>	Lowell Land	✓	✓	I	1
<b>Marion</b>	Charles Gooden	✓			
<b>Marshall</b>	Wyatt Farms	✓	✓	K,V,N,WF,U,C,I,G	193
	Marcus Cope	✓			
	Rick Baker	✓			
<b>Menifee</b>	Danny Ray Townsend	✓	✓	K	175
<b>Mercer</b>	Rose Leigenbooth	✓			

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## Allied services provided to KY Producers (along with associated Retail locations)

...continued...

County	Producer	Services		Retailers	Total Retail Stores	*
		Consultant	Product Placement			
[Refer to legend on last page.]						
Montgomery	Cindy Peake	✓	✓	R	8	
	Glenn Beer	✓				
	Edith Ballesterio	✓				
	Gateway Beef	✓				
	Ruth Hunt	✓	✓	I	4	
Muhlenberg	13 harvestland Family Growers	✓	✓	K,W	397	
Nelson	Jerry Boone	✓	✓	I	5	
	Timothy's Premium Angus	✓				
	Sarah Duncan	✓	✓	I	1	
	Steve Hayden	✓				
	Robert Mayer	✓				
	Joel Bales	✓				
Ohio	48 Harvestland Family Growers	✓	✓	K,W	397	
Oldham	Steve Wilson	✓	✓	V,N,C,I	12	
	Andrew Carrithers	✓				
	Susan Thompson	✓				
	John Bednarski	✓				
Owen	Elk Creek Winery	✓				
Pendleton	Rob Prewitt	✓				
	Kathy Yelton	✓				
Perry	Rebekah Grace	✓	✓	K,L,H,W,S,R,V,T,N,WF,F,U,C,P,I,G	408	
	Don Blackburn	✓				
Pulaski	Tim Tarter	✓	✓	V,N,WF,C,G	11	
	Haney's	✓				
	Southern Belle	✓	✓	C	1	

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## Allied services provided to KY Producers (along with associated Retail locations)

...continued...

County	Producer	Services		Retailers	Total Retail Stores	*
		Consultant	Product Placement			
[Refer to legend on last page.]						
Rockcastle	David King	✓				
	Katherine Hysinger	✓				
Russell	French Valley Farm	✓				
Scott	Kevan Evans	✓	✓	R,V,N,I,WF	39	
	Central KY Growers	✓	✓	K,L,R,V,C	208	
	Susan Harkins	✓				
	Ann Bell Stone	✓	✓	C,I	2	
Shelby	Bill Gallrein	✓	✓	S,R,V,I,C	166	
	Kathy Mejia	✓	✓	I,C,WF,R,V,K	205	
	Larry Harp	✓	✓	I,C,WF,R,V,K	205	
	John Brumley	✓	✓	I,C,WF,R,V,K	205	
	Henry Wells	✓	✓	I,C,WF,R,V,K	205	
	Purnell Farns	✓				
	Patrick Kennendy	✓	✓	I,C,WF,R,V,K	205	
Simpson	Danny Hendricks	✓				
Spencer	Sara Gibbs	✓	✓	I,C,WF,R,V,K	205	
	Sweats Salsa	✓				
Todd	6 Harvestland Family Growers	✓	✓	K,W	397	
Warren	Carl Chaney	✓	✓	U	1	
	Tim Mrchek	✓				
	Bart Anderson	✓	✓	R,V,I	17	
	3 Harvestland Family Growers	✓	✓	K,W	397	

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## Allied services provided to KY Producers (along with associated Retail locations)

...continued...

County	Producer	Services		Retailers	Total Retail Stores	*
		Consultant	Product Placement			
[Refer to legend on last page.]						
Washington						
	Jeff Settles(respectfully)	✓	✓	R	7	
	TR Smith	✓	✓	R	7	
	Danny Spalding	✓	✓	R	7	
	Ray Johnson	✓	✓	R	7	
	Roger Wilkerson	✓	✓	R	7	
	Dudley Tapp	✓				
	Ann Karsner	✓	✓	K,C	4	
	Todd Allen	✓				
	Eddie O'Daniel	✓				
	John Medley	✓	✓	R,V,I	14	
	Eric Ringo	✓				
Wayne						
	Joel Wilson	✓	✓	S	101	
	Curtis harris	✓				
	Ryan Gregory	✓				
Woodford						
	Roger Thacker	✓				
	Cynthia Bohne	✓				
	Ronin Horn	✓	✓	K,R,V,I,C, P	43	
	Mac Weisenberger	✓	✓	L,H,W,R,V,I,C,	67	
	Neil Vasilakes	✓				

**Legend:**

✓	Service Provided	WF	Whole Foods
K	Kroger	F	Fresh Markets
L	Laurel Grocery	U	Land Grant Universities
H	Houchens (Food Giant, IGA, etc)	C	Churchill Downs
W	Walmart	P	Party Marts/Liquor Barns
S	Save-a-lot	I	Independents G+Creation Gardens
R	Remke	N	Natural Independents Stores
V	Valu Mkt	T	Thorton
W	Winkler	M	Meijer
S	Sloan		

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**AGENCY RESPONSE**





## GOVERNOR'S OFFICE OF AGRICULTURAL POLICY

**Steven L. Beshear**  
Governor

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Frankfort, Kentucky 40601  
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agpolicy.ky.gov  
www.kentucky.gov

**Roger Thomas**  
Executive Director

August 11, 2008

The Honorable Crit Luallen  
Auditor of Public Accounts  
105 Sea Hero Rd.  
Frankfort, KY 40502

Dear Ms. Luallen:

Shortly after being appointed Executive Director of the Governor's Office of Agricultural Policy (GOAP) and CEO of the Kentucky Agricultural Development Board (KADB), it became apparent that several financial control and contract management issues had been overlooked. At that time we sought and received authorization from the KADB to pursue an independent review by the Auditor of Public Accounts (APA) of a project in which a possible discrepancy had occurred. We, along with Governor Beshear, are committed to ensuring effective use of the Agricultural Development Funds and many policies have already been implemented that will further this objective.

We appreciate your quick attention to this matter, the diligent work of your staff, their recommendations, and the opportunity to respond to the APA Draft Report: Examination of the Kentucky Agricultural Development Board – Allied Food Marketers West, Inc. Project. The Kentucky Agricultural Development Board is committed to continuing to provide economic investments to the agricultural community of Kentucky and we appreciate the assistance of your staff in helping explore ways to improve the operation of our agency.

Your review includes findings and recommendations. We are providing our response to each of your recommendations herein.

**Recommendation 1.** We recommend KADB legal agreements include provisions that will provide greater protection and oversight capabilities, including the following:

- Termination clause;

- Conflict of interest statements, including limitations on transactions with related parties;
- A requirement for preapproval of subcontractors with scope and cost estimates provided;
- Agreements related to billable charges and fee arrangements, listed in the contract or incorporated by reference to a separate document;
- Clearly defined roles and responsibilities of all parties, including project management and oversight authorities;
- Measurable accountability standards.

**Response 1.**      **We agree with the recommendation. We immediately initiated a review of existing contracts. Further, we began implementing stronger provisions in agreements some of which address the recommendations listed above.**

**The KADB has hired a new general counsel as of August 1, 2008 who will meet with Finance and Administration Cabinet counsel and procurement officials to solicit additional recommendations in order to further strengthen the agreements.**

**Recommendation 2.** We recommend KADB avoid contractual arrangements that create potential conflicts of interest. If applicants can prove that a conflict of interest can be overcome, the justification for approval, as well as additional oversight measures should be approved by legal counsel and documented in the project file.

We also recommend to further reduce the risk of potential conflict of interest, GOAP maintain a file for each of its employees of all external personal and financial conflicts of interests in the agriculture industry. These files should be utilized to ensure that no project analyst or other employee be assigned to projects in which they have a real or perceived conflict of interest.

**Response 2.**      **We agree with this recommendation. Employee files will include disclosures of any personal and financial conflicts of interest within the agriculture community. When assigning employees to review projects these disclosures will be taken into consideration.**

**To further reduce the risk of potential conflicts of interest KADB members are now subject to similar disclosure provisions. Governor Beshear issued Executive Order 2008-**

**454 on May 27, 2008 relating to Standards of Ethical Conduct in the Executive Branch of State Government. A thorough briefing of this Executive Order was provided to the KADB members during their June 27, 2008 board meeting. The KADB is identified as one of the policy-making boards subject to these new standards. This ethics policy has been incorporated into the KADB new member orientation training.**

**Recommendation 3.** We recommend GOAP management and project analysts document all significant decisions and approvals made with project applicants. In order to facilitate this additional documentation, we recommend GOAP institute a project log sheet to be used during each phone conversation and meeting with applicants and recipients. It is not necessary to document routine discussions, but all conclusions that modify the scope or clarify definitions of the legal agreement should be documented and maintained on file.

We also recommend management and project analysts document cost estimates of any modifications approved, and GOAP management establish a policy for modifications that require input from general counsel and/or the executive director.

**Response 3.** **We agree with this recommendation and will work towards implementation. Internal policies and paperwork are currently being reviewed with newly hired general counsel.**

**Recommendation 4.** We recommend GOAP improve monitoring procedures by:

- Developing a checklist for each project file to document the monitoring procedures outlined and performed for that specific project. The checklist can be tailored to the type of project and dollar amount of funding awarded, and included a variety of monitoring procedures and accountability measures, such as a review of the standard quarterly / annual reports for budgetary review, periodic on-site monitoring, inspection of a sample of detailed receipts, and a final project report that provides an overall project evaluation.
- Documenting a list of unallowed expenses and establishing guidelines for reasonable and necessary expenses and providing this information to all project applicants. This list should be periodically reviewed, updated, and modified based on the type of contract as needed.
- Expanding the staffing resources for compliance related functions to devote more time for detailed monitoring.

- GOAP may consider part-time assistants or interns to help with model programs, and consider utilizing project analysts for some monitoring functions outside of their own district assignment to maximize the use of their workforce. Project analysts should not be assigned to monitor projects within their own districts.

We also recommend GOAP communicate clear expectations regarding the acceptance of gifts and gratuities, including meals, in order to ensure compliance with KRS 11A.045. This policy should be communicated to all GOAP employees, as well as to KDA and other state agencies receiving KADB funding.

**Response 4.**

**Although the GOAP maintains a checklist for each project, we will work to enhance the checklist to incorporate more stringent and detailed monitoring and accounting procedures.**

**We will work with the Finance and Administration Cabinet to develop guidelines for disallowed expenses and reasonable and necessary expenses that are consistent with others in state government.**

**We appreciate the recommendation for expanded staffing resources for compliance-related functions. Current management is aware of the need for additional staffing resources and is pursuing ways to refocus existing staff on compliance issues. In addition to the refocusing of existing staff, management was able to secure additional staffing in the 2009-2010 Executive Branch Budget that will provide compliance support.**

**We respectfully disagree that project analyst should not be assigned to monitor projects within their own districts. Project analysts' knowledge and experience with a project would go unutilized and be a detriment to successful oversight. We believe that the implementation of the conflict of interest disclosure recommended earlier in this audit will provide sufficient measures to prevent project analysts from being assigned to projects in which there may be any potential conflicts.**

**All GOAP employees are subject to and are provided with the Executive Branch Code of Ethics. In addition, management takes advantage of opportunities to remind employees of the provisions related to the acceptance of gifts and gratuities. Most recently, this provision was reviewed at the July 15, 2008**



**GOAP staff meeting. New employee ethics training will be coordinated through the GOAP Ethics Officer.**

**Recommendation 5.** We recommend KADB improve monitoring and make project accountability by GOAP a priority. The lack of reliable financial reporting made it difficult for KADB to meet its statutory requirement noted in KRS 248.709 of developing criteria to evaluate the success of the board's programs. KADB made a positive step toward improving accountability by implementing a quarterly recipient review committee for Allied. However, this committee did not receive adequately detailed information to provide strong oversight. Also, by meeting with Allied quarterly, the committee could not make timely decisions had they become necessary, and thus is dependent upon GOAP providing more routine monitoring and communicating serious concerns in the interim.

**Response 5.** We agree with the recommendation. GOAP's general counsel will serve as Chief Compliance Officer and will work with other staff members to strengthen monitoring and accountability of both existing and future projects.

**In an effort to strengthen the Recipient Review Committee process, GOAP staff will recommend a change to the KADB's Recipient Review Committee policy. Currently policy states that the committee "...shall not meet more than quarterly." At the August 2008 KADB meeting, GOAP will recommend that the committee meet as needed. This change will enable the KADB and the Recipient Review Committee to make more timely decisions.**

We appreciate the hard work of your staff and their thorough review and recommendations. As the KADB continues to provide investment in the Commonwealth's agricultural community, we will work to improve our policies and procedures in order to maintain a high level of confidence in our programs.

Sincerely,

A handwritten signature in dark ink, appearing to read "Roger Thomas", written in a cursive style.

Roger Thomas  
Executive Director, Governor's Office of Agricultural Policy  
CEO, Kentucky Agricultural Development Board